

**From:** Jonathan H. Bari  
**To:** Renata Hesse  
**Date:** 1/28/02 3:23pm  
**Subject:** Microsoft Settlement

Dear Renata,

Pursuant to the Tunney Act, attached please find our comments on the Revised Proposed Final Judgement.

Thank you.

Jon

----- (NOTE NEW OFFICE ADDRESS AS OF 11/21/01)

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CNN Headline News calls CATAVULT - "one site that can get you in everywhere..."

BusinessWeek calls CATAVULT, "An Open Sesame for the Whole Web."

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**BEFORE THE UNITED STATES DEPARTMENT OF JUSTICE**

UNITED STATES OF AMERICA

Plaintiff,

v.

MICROSOFT CORPORATION,

Defendant.

Civil Action No. 98-1232 (CKK)  
United States District Court for the  
District of Columbia

STATE OF NEW YORK *ex rel.* Attorney  
General ELIOT SPITZER, *et al.*,

Plaintiffs,

v.

MICROSOFT CORPORATION,

Defendant.

Civil Action No. 98-1233 (CKK)  
United States District Court for the  
District of Columbia

**COMMENTS OF CATAVULT ON THE REVISED PROPOSED FINAL JUDGMENT**

## INTEREST OF THE COMMENTER

Given that Microsoft's .Net Passport is the heart of Windows XP, Microsoft's new Operating System that was officially launched on October 25, 2001, Catavault, a software company addressing online identification and authentication, unfortunately finds itself in the cross-hairs of the most powerful software company in the world, since Microsoft has tied its .Net Passport to Windows XP. Pursuant to the Tunney Act, this document sets forth Catavault's comments on the Revised Proposed Final Judgement because we feel that competing products such as Catavault will still unfortunately be set at a disadvantage which is not related to price or quality. If the Revised Proposed Final Judgement is accepted as is, the result will be a weakening of effective competition in the market, a reduction in consumer choice and less technological innovation, generally speaking and specifically to online identification and authentication.

Catavault has developed, commercially licensed and deployed patent pending software that is both complementary and competitive with Microsoft .Net Passport in online identity and authentication services. Although Microsoft's September 20, 2001 announcement that a future version of .Net Passport will be federated,<sup>1</sup> and thus may be interoperable with rivals' services, we believe that this in no way alters the extremely serious concerns articulated herein. Moreover, in spite of the Revised Proposed Final Judgement announced between the United States Department of Justice, nine states Attorneys General and Microsoft Corporation, Catavault believes that this in no way alters the extremely serious concerns articulated herein. As such, Catavault has been encouraged that various states Attorneys General still have the resolve and resources necessary to continue the fight in ensuring conduct remedies that are timely, effective, certain and practical when it comes to curbing Microsoft's recidivistic behavior.

While these Tunney Act comments were prepared from the heart so to speak of the entrepreneurs managing Catavault, Catavault has been working to promote vigorous competition in computer industry platforms and gateways with our antitrust counselors from Morgan, Lewis and Bockius including Mr. Willard K. Tom based in Washington, D.C. and Mr. Julian M. Joshua based in Brussels.

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<sup>1</sup> See <http://www.microsoft.com/presspass/press/2001/sep01/09-20PassportFederationPR.asp>.

## **CATAVAULT OVERVIEW**

Catavault is a pioneer in the online user identification and authentication space. Catavault's technology powers the "All Access Pass to the Internet," and it allows users to access more than 3,500 sites ranging from Amazon.com to ZDNet, a couple of orders of magnitude more than Microsoft's .Net Passport currently enables access to, without the need to remember all of their authentication credentials for those sites. Unlike .Net Passport which is only accessible from a PC, Catavault is accessible from a PC, PDA, Mobile Phone and Set-top Box, so users can access their information from any device, at any time and from anywhere. CNN Headline News has called Catavault - "one site that can get you in everywhere..." BusinessWeek has called Catavault, "An Open Sesame for the Whole Web." Despite these arguably superior features of its services, Catavault is severely endangered by the steps Microsoft is taking to ensure that .Net Passport becomes the dominant occupant of the online identity and authentication space. Accordingly, Catavault is endangered by the Revised Proposed Final Judgement. The remedial principle is straightforward enough: the remedy should unfetter a market from anticompetitive conduct, . . . terminate the illegal monopoly, deny to the defendant the fruits of its statutory violation, and ensure that there remain no practices likely to result in monopolization in the future.<sup>2</sup> However, in spite of the overwhelming en banc victory on liability, the Revised Proposed Final Judgement does little to ensure that conduct remedies are timely, effective, certain and practical in curbing Microsoft's anti-competitive behavior.

## **NETWORK CHARACTERISTICS & MICROSOFT'S HAILSTORM STRATEGY**

Microsoft fully recognizes that, because of the network characteristics of the industry, only subtle uses of its monopoly position are necessary in order to gain an unwarranted, but insuperable dominance in this field. Indeed, its choice of "HailStorm" as a metaphor speaks volumes. As you may know, with each updraft in the natural weather-related occurrence of a hail storm, hail stones get larger as more water molecules attach to the crystalline structures of the hail stones. Similarly, Microsoft makes its monopoly position more impregnable with every adjacent space it dominates. Each layer creates another multiple-level entry problem for potential competitors, as described in the United States Department of Justice's 1984 Merger

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<sup>2</sup> United States v. Microsoft Corp., slip op. at 99-100, No. 00-5212 (D.C. Cir. June 28, 2001), *quoting* Ford Motor Corp v. United States, 405 U.S. 562, 577 (1972); United States v. United Shoe Mach. Corp., 391 U.S. 244, 250 (1968).

Guidelines to which the United States Federal agencies still refer in non-horizontal matters. Figure 1 is a visual representation of the troubling processes that Catavault sees at work with respect to a monopolist bundling its own applications to its dominant Operating System.

As reported in *The Wall Street Journal* on September 20, 2001, Microsoft changed the name of its HailStorm initiative to ".Net My Services" - possibly because they realized that its very name, HailStorm, has strong whiffs of antitrust violations.

One can argue that network effects require a lock-in mechanism. However, the traditional lock-in mechanism is access to complements. Some of the services offered by Catavault and .Net Passport require cooperation from third party Internet site(s). If .Net Passport has a much larger number of users, gained through the use of its operating system monopoly, then why would the sites want to work with Catavault? If the sites cease to work with Catavault, then why would users find Catavault attractive? These questions and their answers are paramount to understanding how market signaling and network effects work towards the monopolist's advantage when it ties its own applications to its dominant Operating System.

## **NETSCAPE — FRUITS OF MICROSOFT'S STATUTORY VIOLATIONS**

Most harmful of all is the message that Microsoft's actions have conveyed to every enterprise with the potential to innovate in the computer industry. Through its conduct toward Netscape, IBM, Compaq, Intel and others, Microsoft has demonstrated that it will use its prodigious market power and immense profits to harm any firm that insists on pursuing initiatives that could intensify competition against one of Microsoft's core products. Microsoft's past success in hurting such companies and stifling innovation deters investment in technologies and businesses that exhibit the potential to threaten Microsoft. The ultimate result is that some innovations that would truly benefit consumers never occur for the sole reason that they do not coincide with Microsoft's self-interest.<sup>3</sup>

Accordingly, When Microsoft destroyed Netscape as a potential rival platform, it did more than achieve dominance in browsers. It also prevented rival applications developers from playing Microsoft off against Netscape in the battle to ensure the survival of their applications programs and services. If Netscape and/or other browser/middleware platform software had

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<sup>3</sup> Judge Thomas Penfield Jackson's Finding of Fact, 412th and final paragraph, November 5, 1999.

survived as a serious competitor to Microsoft, competitive pressures would have forced one or more platforms to carry Catavault, because doing so would have provided a competitive advantage. The platform itself would have become more attractive if, through accessing Catavault, users were freed from cumbersome authentication procedures on a much larger number of sites. That competitive pressure is now gone. Thus, Catavault's current predicament flows directly from Microsoft's earlier unlawful acts against Netscape.

## **MARKET EXPECTATIONS STIFLE INNOVATION AND COMPETITION**

Moreover, the very public humbling of an 85 percent market share player like Netscape in itself creates market expectations that where Microsoft announces an intention to dominate a strategic space, it will succeed in doing so. .Net Passport occupies a strategic space as the on-ramp to the Internet as illustrated in Figure 2, and Microsoft has been quite public about that fact as has been reported in articles in *The Industry Standard*.<sup>4</sup> Consequently, merchants, investors, and other marketplace participants become highly resistant to dealing with Microsoft's competitors in such spaces. For example, Benjamin D. Black, a principal of the Rosewood Venture Group, a U.S. venture capital firm in San Francisco, California has stated, "I still won't invest in companies that are directly in front of Microsoft's development path."<sup>5</sup> And Stewart Alsop, a general partner of New Enterprise Associates, a Silicon Valley venture capital firm in the U.S., has been quoted as saying, "The most common question for potential investors is: 'What about Windows XP?' You can still compete but if Microsoft bundles it in Windows it makes it much more difficult for any kind of innovation that is in Microsoft's path."<sup>6</sup> Thus, in this sense, too, Microsoft's earlier unlawful acts against Netscape directly cuts Catavault off from access to important complements.

To that end, one could argue that the competition is ultimately not for the end-user, but for the online service providers who actually pay for online identity and authentication services. Signing up 200 million Hotmail accounts gives Microsoft a huge critical mass of users, but what does it do to get third party sites to work with .Net Passport? To answer this effectively, one must understand that having so many users signals to the marketplace that Microsoft will

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<sup>4</sup> <http://www.thestandard.com/article/0,1902,27685,00.html>.

<sup>5</sup> *The New York Times*, September 7, 2001, Competitors See a Giant That Is Now Largely Unfettered, by Michael Brick.

dominate online identity and authentication services. Moreover, these third party businesses are motivated to work with Microsoft based on the marketing support that Microsoft can provide them — thus creating value propositions from Microsoft's monopoly position. If third party businesses believe that Microsoft will also succeed in using its Operating System monopoly to push Catavault and/or others aside in terms of subscribers or utilities, then third party firms will not have an incentive to work with Catavault. As former United States Deputy Assistant Attorney General Carl Shapiro has described in his writings, expectations play a very large role in network markets.<sup>7</sup>

### **MAKING .NET PASSPORT THE DE FACTO IDENTITY SERVICE IN WINDOWS XP**

Microsoft has taken a number of steps to ensure, and to make consumers believe, that having a .Net Passport account is necessary in order to access features of Windows XP and/or other Microsoft goods and services. Indeed, the press, encouraged by Microsoft, has come to the conclusion that Microsoft .Net Passport "will be the exclusive identity service on the new Windows XP operating system. Any XP user who wishes to access key services such as Windows Messenger (for Instant Messaging) will have to register for a Passport."<sup>8</sup>

Microsoft has not achieved its claimed 2000 million .Net Passport subscribers by offering a superior service. (Competitive market research indicates that .Net Passport is currently accepted by only about 35-70 sites, most of which are owned by Microsoft, have received substantial Microsoft investment or partnered with Microsoft in some sort of business arrangement.) Instead, it has done so by these kinds of suggestions of inevitability and by automatically opening .Net Passport accounts for all Hotmail and MSN users, and even hinting at future integration and potential incompatibilities. Thus, in published reports regarding .Net Passport 2.0, it is stated, "...with this release, Hotmail will move to the Passport code base for easier integration."<sup>9</sup>

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<sup>6</sup> *The New York Times*, September 7, 2001, Pendulum Swings to Microsoft, But the Degree Remains Unclear, by Steve Lohr.

<sup>7</sup> Speech by Carl Shapiro, Deputy Assistant Attorney General, Antitrust Division, United States Department of Justice. American Law Institute and American Bar Association, "Antitrust/Intellectual Property Claims in High Technology Markets," San Francisco, California, January 25, 1996.

<sup>8</sup> Source: <http://www.thestandard.com/article/0,1902,27685,00.html>, attached.

<sup>9</sup> Source: <http://www.wininformant.com/Articles/Index.cfm?ArticleID=22174>, attached.

Catavault experienced this directly in early September 2001 when a Catavault employee tried to access the latest release candidate of XP. First, he learned that one could not get the latest preview of XP online without a .Net Passport account.<sup>10</sup> Then, after downloading that version of XP and rebooting, he got a blank desktop, but in the system tray in the bottom right, a message popped up that said:

"Add your .NET Passport to Windows XP!

You've just connected to the Internet. You need a Passport to use Windows XP Internet communications features (such as instant messaging, voice chat, and video), and to access .NET-enabled services on the Internet.

Click here to set up your Passport now."

When he clicked, it went to the .NET Passport Wizard to let him sign up for Passport.

Thus, whether or not there are actual incompatibilities, Microsoft has been representing to users that they must sign up for .Net Passport in order to access key XP features or other Microsoft services. In a network business, that may be all Microsoft needs to maintain and extend its dominance to this space as well. These network characteristics undoubtedly underlie some of the "vaporware" aspects of Microsoft's dramatic announcements but slow rollout. We have already mentioned how small the number of third party sites accepting .Net Passport is. In the same vein, ZDNet has reported that American Express has yet to sign a contract with Microsoft for HailStorm services. This despite the fact that Microsoft touted American Express as a partner at the very announcement of the HailStorm initiative, by featuring American Express' Chief Information Officer in that announcement.<sup>11</sup>

## **PROPOSED CONDUCT REMEDIES TO CURB ANTI-COMPETITIVE PRACTICES**

If there is no efficiency justification for Microsoft's tactics such as bundling and/or market signaling, they may be acts of monopolization in themselves. But regardless of whether they are or not, the current situation flows directly from Microsoft's earlier unlawful acts against Netscape. While one can never know with certainty exactly what that but-for world would have been had Netscape survived, it was reasonably certain that, for some significant period of time, there would have been a competitive struggle between Microsoft and Netscape as alternative nuclei around which other providers of applications and services would coalesce. Both would

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<sup>10</sup> Source: <http://www.microsoft.com/windowsxp/preview/systemreq.asp>.

<sup>11</sup> <http://www.zdnet.com/zdnn/stories/news/0,4586,5096385,00.html>.



seek to commoditize the other's space. If Netscape gained the upper hand, multiple operating systems would become available to computer users. If Microsoft gained the upper hand, multiple browsers would become available. Consequently, any remedy for those earlier acts needs to include some kind of mandated intra-system competition to take the place of the competition that would have existed between the two systems to add attractive applications through a Ballot Screen with choices for online identity and authentication services such as Catavault.

We have given a great deal of thought to what order language would be needed to implement the concept of a Ballot Screen. Following is the rationale and the result can be found in Figure 3 with the language marked as to revisions. It uses Microsoft's inclusion of middleware products in its operating system software as the benchmark for what types of products should be included, with the slight modification that it remedies the continuing effects of past inclusions as well as remedying the effects of future inclusions. As you will see, there is a provision for approval by some entity, corresponding to Commission approval in the AOL Time Warner order, in order to ensure that the competing products are serious competitors to Microsoft. In the case of online identity and authentication, the seriousness of the competition can be measured by the number of sites, users, and devices accessed by the competitor. These metrics could be written into the order if desired, but in any event the existence of available metrics would ensure that the entity charged with approval would have an objective way of exercising that discretion. As you will also see, when we reviewed Judge Jackson's order, we concluded that online identity and authentication service software would fit comfortably into the definition of "middleware," but for the avoidance of doubt, we included it specifically in the list of examples. In addition to offering services via communications interfaces as now occurs, it is entirely possible that in the future, programmers of sites or of programs used to build sites will write software built upon a Catavault platform.

We have also given further thought to the Department of Justice's observation that a possible standard for relief is that it should be aimed at opening the operating system market to competition. After reflection, we believe that our proposed Ballot Screen relief does in fact further that goal, but that such a standard is nonetheless wrong, in spite of that standard appearing in the Department of Justice's September 6, 2001 press release.

The relief we propose does further the goal of operating system competition, because allowing Microsoft to use its operating system monopoly to obtain a dominant position in the authentication gateway to the Internet will mean the creation of yet another applications barrier to entry, because it will be extremely difficult to police the ways in which Passport could be used to favor Windows if a credible threat to Windows arose.

There is, however, a more fundamental issue: the proper standard must be to restore the competitive conditions that would have existed but for the illegal conduct. It is, of course, too late to revive Netscape as a credible threat to Microsoft's operating system monopoly. One approach might be, as the Department of Justice once proposed, to find in Microsoft's applications software -- particularly its dominant Office suite -- a sufficiently dangerous competitive threat to the operating system monopoly. As in the competition between Microsoft and Netscape in the but-for world, the point of that remedy was not to assure ultimate, long-term competition in operating systems. The operating system company might win the competitive struggle, and ultimately maintain its monopoly position through lawful means. The point of the remedy was the competitive struggle itself. That remedy was imperfect, as are all the alternatives. But for better or worse, it is now off the table.

Whatever replaces it, the goal should not be to assure ultimate, long-term competition in operating systems. The but-for world did not do so. Microsoft might well have won the competitive struggle, and maintained its monopoly. The point of the Netscape threat to the operating system monopoly was that Microsoft had to compete with better products and prices, and in the meantime the rest of the computer industry would be vigorously competitive and innovative, and might nurture the next threat to the surviving monopolist. It is the strangling of that dynamic from which the market must be unfettered, and it is Microsoft's freedom from that dynamic that constitutes the "fruits of its statutory violation." At this point in the evolution of the computer industry, after Microsoft's misconduct, it might well be a hopeless task to restore competition in operating systems.

It is not too late, however, to restore the competitive dynamic that ensured that, while Microsoft battles its chief rivals in the most strategic battleground at any given time, innovators in the next strategic space could play one against the other in order to survive. At the moment, the inter-system competition that Netscape represented is gone, and the Department of Justice is no longer seeking to have competition from Microsoft Office take its place. Thus, the temporary stopgap by which the next strategic space can develop must be intra-system competition, or "must-carry." That will revive some of the competitive dynamic that Microsoft has cut off, and allow competition to flourish in - and on the other side of - those gateways.

Ergo, just as Microsoft agreed to change its digital imaging features to give users easier access to digital imaging software from a number of providers such as Kodak, not just those affiliated with Microsoft, so there needs to be a requirement that Microsoft incorporate Catavault (and other online identity and authentication services that may arise) into XP as a complementary and competitive service. Thus, doing some kind of a "Ballot Screen" for consumers to select which online identity and authentication service they would like may be as close as one can get to the competitive landscape that would have existed but for Microsoft's already adjudicated unlawful conduct.

In addition, of course, one would need to prohibit Microsoft from introducing incompatibilities, to forbid Microsoft from making use of .Net Passport as a prerequisite to use other Microsoft goods and services, and so forth. Otherwise, the need to sign up with .Net Passport to get the XP preview is likely to continue to be the typical pattern for accessing anything that Microsoft can control or influence.

## **MICROSOFT'S FEDERATED ANNOUNCEMENT & INTERNET TRUST NETWORK - ITS EFFECTS AND RELATION TO FEAR, UNCERTAINTY & DOUBT**

A "Ballot Screen" remedy would be far superior to waiting to see how Microsoft's latest federated announcement plays out. As the Department of Justice well knows, a "fear, uncertainty and doubt" strategy relies heavily on the passage of time and the uncertainty of the future. (This is undoubtedly why Microsoft has been making every effort to delay judicial and legislative proceedings in the United States.) As of January 28, 2002, Catavault has neither been invited to any Microsoft developers conference yet, nor has it learned of any developers conference yet, albeit Catavault has informed Microsoft about its potential willingness to

participate in the conference. Additionally, XP has already been launched with an aggressive marketing campaign and with .Net Passport as the exclusive online identity and authentication service. .Net Passport will have a huge user base that will undoubtedly get larger between now and the time that any Microsoft federation conference or any competitive and/or complementary solution such as the Liberty Alliance initiated by Sun Microsystems produces any tangible results in the marketplace. The agenda of the federated conference and other like it such as the Liberty Alliance may be to develop standards for implementation of online user identification and authentication services, and in the case of Microsoft's Internet Trust Network, built upon a technology platform of Microsoft's choosing, regardless of consumer preferences. Following that developers' conference, there may be a long period of back-and-forth over technical standards. Next may come a period in which Microsoft sows uncertainty about the extent to which other services are fully interoperable, perhaps because of peculiarities in Microsoft's implementation of the common standard. During all that time, .Net Passport will become more and more entrenched, regardless of consumers' preferences as to the features and scope of competing online user identification and authentication services.

Industry pundits used to subscribe to the notion that first mover advantage was the most important mission of many new technology ventures. However, based on present market conditions, we argue that it has nothing to do with first mover advantage anymore; rather it has everything to do with the concept of last man standing. Accordingly with over US \$36 billion in cash reserves on hand, Microsoft is well positioned to be the last man standing in many industries including online identity and authentication.

## **PROBLEMS WITH THE REVISED PROPOSED FINAL JUDGEMENT**

While there are many troubling issues with the Revised Proposed Final Judgement, two of the more salient problems for the online identity and authentication sector involve the following terms and provisions:

- OEMs - The fact is that Original Equipment Manufacturers (OEMs) are a sub-optimal source to serve as an adequate check and balance on Microsoft's anti-competitive actions. For example, the provisions that allow OEMs to have greater freedom to select which software to use and not to use do absolutely nothing to protect consumer choice and technological innovation.

Thus, providing the OEMs greater freedom as a conduct remedy against Microsoft is meaningless today given consolidation in the PC industry, slumping PC sales, depressed PC margins, and the fact that the OEMs do not want to bite the hand that feeds them - Microsoft.

Moreover, the OEMs know very well that small companies such as Catavault cannot afford to compete against Microsoft, both in terms of operations and marketing. Case in point, Windows XP launched on time because Microsoft lobbied that XP would help revive slumping PC sales, and Microsoft is spending approximately US \$250 million just on marketing for XP. As such, OEMs do not necessarily want to bet on smaller players which find themselves in the cross-hairs of Microsoft - thus consumer choice and technological innovation are still harmed.

- AUTHENTICATION LOOPHOLE - The following provision from the proposed settlement seems to be the veritable loophole large enough to drive a truck through, particularly affecting Catavault and other online identity and authentication services.

J. No provision of this Final Judgment shall:

1. Require Microsoft to document, disclose or license to third parties: (a) portions of APIs or Documentation or portions or layers of Communications Protocols the disclosure of which would compromise the security of anti-piracy, anti-virus, software licensing, digital rights management, encryption or authentication systems, including without limitation, keys, authorization tokens or enforcement criteria; or (b) any API, interface or other information related to any Microsoft product if lawfully directed not to do so by a governmental agency of competent jurisdiction.<sup>12</sup>

Identification and authentication is singled out for a loophole to free Microsoft's .Net Passport from scrutiny and permit Microsoft to bind a universal identification and authentication service utility to its monopoly operating system without scrutiny under the Revised Proposed Final Judgement. By permitting Microsoft to withhold key parts of encryption, digital rights management, authentication, and other security protocols, the Revised Proposed Final Judgement effectively clears the way for the desktop monopolist to

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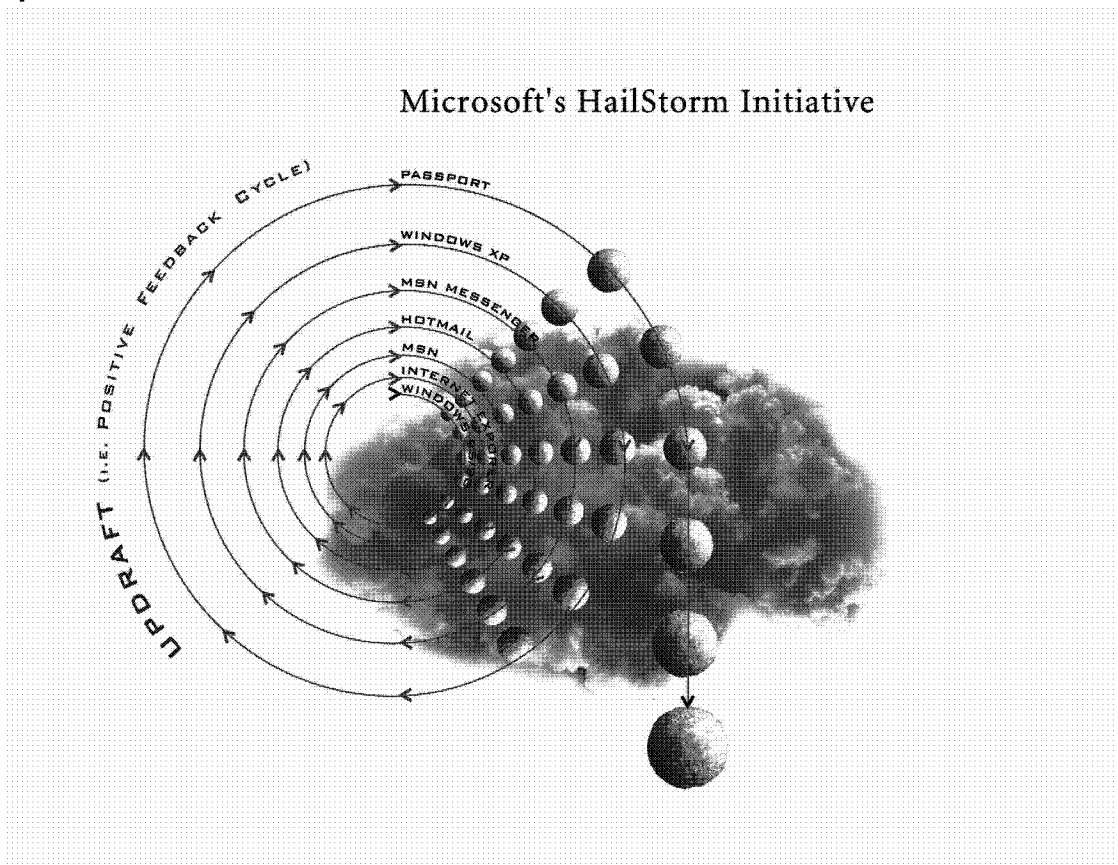
<sup>12</sup> <http://www.usdoj.gov/atr/cases/f9400/9462.htm>

the Web-services monopolist in a distributed computing environment. The Revised Proposed Final Judgement could hardly try to place a clearer stamp of approval on an expansion of the scope of an illegally maintained monopoly.

## **CONCLUSION**

The Revised Proposed Final Judgement agreed to by the United States Department of Justice, the Attorneys General of nine states and Microsoft Corporation does not attain its goals of curbing Microsoft's recidivistic behavior in maintaining and extending its operating system monopoly into Web-services such as online identification and authentication, which Microsoft has bet will be the next gateway to the Internet. Specifically, the Revised Proposed Final Judgement does not provide adequate incentives across constituent bodies and penalties for Microsoft to ensure that the Revised Proposed Final Judgement goals are attained. Moreover, the lenient conduct remedies imposed on Microsoft are essentially a slap on the wrist for its illegal conduct and anti-competitive practices. Unfortunately, technological innovation and consumer choice will continue to be harmed, and this will be exacerbated in challenging economic conditions if the Revised Proposed Final Judgement is accepted as is. As such, the Revised Proposed Final Judgement needs to be revised significantly if it is to have any real impact in the marketplace in curbing Microsoft's recidivistic behavior. Specifically, as it pertains to the heart of Windows XP and Microsoft's goal of dominating online identification and authentication with .Net Passport, we believe quite passionately that implementing a Ballot Screen for users to choose which identification and authentication service that they would like would go a long way to providing a conduct remedy that was more timely, effective and certain.

Figure 1



**"The world of operating systems becomes more homogenous over time. Today something like 85 percent of the computers on the planet run the same operating system [Microsoft's]. There is sort of a positive feedback cycle here. If you get more applications, it gets more popular, if it gets more popular, it gets more applications."**

--Bill Gates keynote address, Conference on Internet and Society at Harvard in May 1996; *World War 3.0* by Ken Auletta.

On June 28, 2001, the District of Columbia Court of Appeals unanimously held that Microsoft engaged in unlawful monopolization. Notwithstanding Judge Jackson's ruling and the appellate ruling, Microsoft prominently announced its major corporate initiative called HailStorm in March 2001; the very choice of HailStorm as a name serves as a metaphor for a positive feedback cycle in Bill Gates' opinion or network effects and increasing returns in an antitrust perspective.

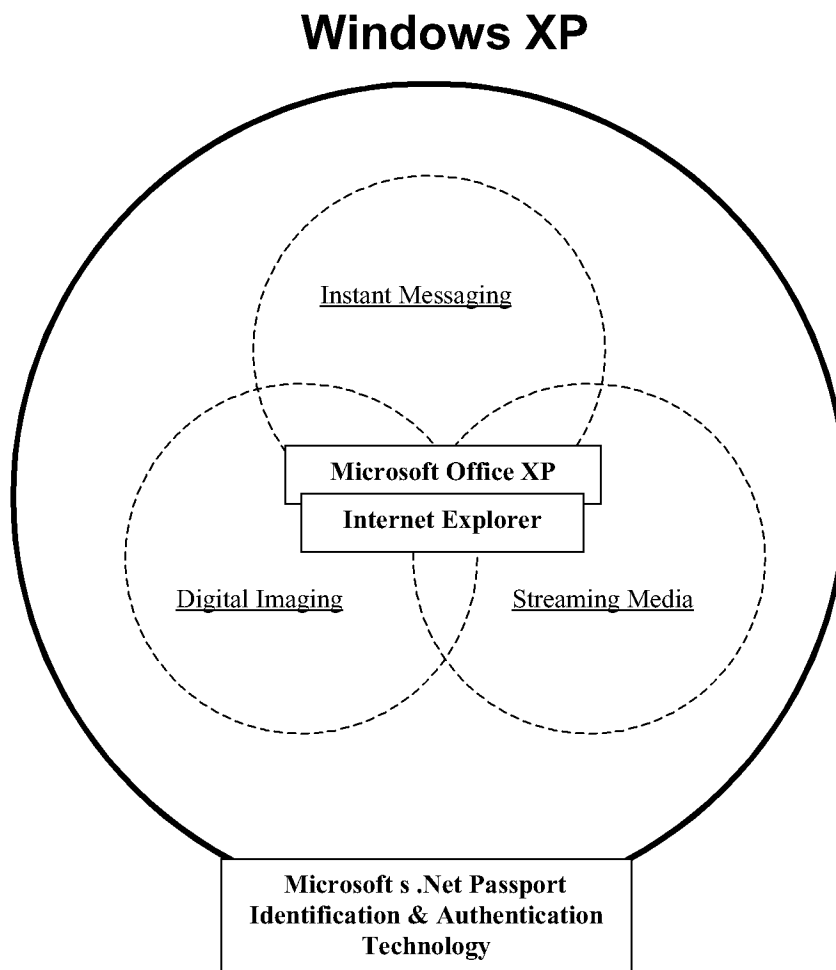
**The heart of HailStorm is based on .Net Passport, Microsoft's proprietary online identification and authentication service. This market signaling transcends into Microsoft's strategy and tactics to gain market advantage in new sectors using .Net Passport. .Net Passport is the exclusive online identification and authentication service on Windows XP. Accordingly, .Net Passport will be the de facto online identification and authentication service which will limit consumer choice and undermine innovation.**

As reported in *The Wall Street Journal* on September 20, 2001, Microsoft changed the name of HailStorm to ".Net My Services" - possibly because they realize that its very name - HailStorm - has strong whiffs of antitrust violations.

Note: In its natural weather-related occurrence, hail stones are large frozen raindrops produced by intense thunderstorms. As the frozen drops fall, liquid water freezes onto them forming ice pellets that continue to grow as more and more droplets accumulate. Upon reaching the bottom of the cloud [symbolic for the Internet], some of the ice pellets are carried by the updraft back up to the top of the cloud. As the ice pellets once again fall through the cloud, another layer of ice is added and the hail stones grow even larger. Typically the stronger the updraft, the more times hail stones repeat this cycle and consequently, the larger the hail stones grow. Once the hail stones become too heavy to be supported by the updraft, they fall out of the cloud toward the surface. The hail stones reach the ground as ice since they are not in the warm air below the thunderstorm long enough to melt before reaching the ground. And as one knows, you should take cover from a hail storm...

Figure 2

**Microsoft's .Net Passport online identification & authentication technology controls the gateway to all applications in Windows XP**



***It's our goal to have virtually everybody who uses the Internet to have one of these Passport connections*** - Bill Gates

Source: *The Industry Standard* - July 3, 2001  
<http://www.thestandard.com/article/0,1902,27685,00.html>

While digital photography, instant messaging and streaming media all are very important issues to constituents such as Kodak, AOL Time Warner and Real Networks respectively, the backbone to Microsoft's HailStorm (renamed .Net My Services) initiative and full utilization of Windows XP is the Microsoft .Net Passport identification and authentication service. Microsoft has stated that .Net Passport will be the exclusive Internet identity service on Windows XP, and Passport will be required to utilize some or all of the features noted above. Thus, even if competition in those areas is assured, Microsoft will still hold the real keys to access and conceivably will be able to use its .Net Passport monopoly to direct traffic away from competing digital photography, instant messaging and streaming media applications.

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### Figure 3 Proposed Order (Marked with changes)

3g. ~~Binding~~ Restriction on Including Middleware Products in Operating System Products. Microsoft shall not, in any Operating System Product distributed six or more months after the effective date of this Final Judgment, ~~Bind~~ include any Middleware Product ~~in~~ a Windows Operating System unless:

i. that Operating System also includes at least two (2) comparable Middleware Products offered by non-affiliated firms approved by the [Antitrust Division] [Department of Justice] [Court] [Trustee] or Microsoft demonstrates to the satisfaction of [\_\_\_\_\_] that fewer than two such products exist, in which case Microsoft shall include all that exist. The option of using such non-affiliated products shall be displayed to the user on terms no less favorable than those accorded to the Microsoft products.

ii. Microsoft also offers an otherwise identical version of that Operating System Product in which all means of End-User Access to ~~that~~ those Middleware Products can readily be removed (a) by OEMs as part of standard OEM pre-installation kits and (b) by end users using add-remove utilities readily accessible in the initial boot process and from the Windows desktop.~~;~~ ~~and~~

~~iii. when an OEM removes End-User Access to a Microsoft Middleware Product from any Personal Computer on which Windows is preinstalled, the royalty paid by that OEM for that copy of Windows is reduced in an amount not less than the product of the otherwise applicable royalty and the ratio of the number of amount in bytes of binary code of (a) the Middleware Product as distributed separately from a Windows Operating System Product to (b) the applicable version of Windows.~~

3g . Middleware Products Included in Previously Distributed Operating System Products. If Microsoft has, in any Operating System Product distributed less than six months after the effective date of this Final Judgment, included any Middleware Product in a Windows Operating System, it shall within six months after the effective date of this Final Judgment:

i. release a version of its most recent Operating System that includes at least two (2) comparable Middleware Products offered by non-affiliated firms approved by the [Antitrust Division] [Department of Justice] [Court] [Trustee], unless Microsoft demonstrates to the satisfaction of [\_\_\_\_\_] that fewer than two such products exist, in which case Microsoft shall include all that exist. The option of using such non-affiliated products shall be displayed to the user on terms no less favorable than those accorded to the Microsoft products.

ii. offer an otherwise identical version of that Operating System Product in which all means of End-User Access to those Middleware Products can readily be removed (a) by OEMs as part of standard OEM preinstallation kits and (b) by end users using add-remove utilities readily accessible in the initial boot process and from the Windows desktop.

7q. Middleware means software that operates, directly or through other software, between an Operating System and another type of software (such as an application, a server Operating System, or a database management system, including such Operating Systems and database management systems on an Internet site) by offering services via APIs or

Communications Interfaces to such other software, and could, if ported to or interoperable with multiple Operating Systems, enable software products written for that Middleware to be run on multiple Operating System Products. Examples of Middleware within the meaning of this Final Judgment include Internet browsers, online identity and authentication service software, e-mail client software, multimedia viewing software, Office, and the Java Virtual Machine. Examples of software that are not Middleware within the meaning of this Final Judgment are disk compression and memory management.

r.       Middleware Product means

        i.       Internet browsers, e-mail client software, multimedia viewing software, instant messaging software, online identity and authentication service software, and voice recognition software, or

        ii.      software distributed by Microsoft that —

                (1)     is, or has in the applicable preceding year been, distributed separately from an Operating System Product in the retail channel or through Internet access providers, Internet content providers, ISVs or OEMs, and

                (2)     provides functionality similar to that provided by Middleware offered by a competitor to Microsoft.